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In the Supreme Court of the United States

OCTOBER TERM, 1969

No. 1073

FORD M. MACELVAIN, ET AL., PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 27–33) is reported at 417 F. 2d 1134. The opinion of the district court (Pet. App. 22–26) is reported at 299 F. Supp. 1352.

JURISDICTION

The judgment of the court of appeals was entered on November 4, 1969. The petition for a writ of certiorari was filed on January 13, 1970. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether petitioners were properly enjoined from selling, without registration under the Securities Act of 1933, quitclaim deeds to offshore oil lands coupled with a promise to litigate the validity of the title to the land for the benefit of the purchasers.

2. Whether in the injunction proceeding the district court properly required the defendants, pursuant to the Federal Rules of Civil Procedure, to respond to requests for admissions and to take the witness stand.

3. Whether petitioners' constitutional rights were abridged by the court of appeals' decision to place this case on its summary calendar, and thereby to consider the merits of the appeal on the basis of the record and briefs without oral argument.

STATUTE INVOLVED

Sections 5(a) and 5(c) of the Securities Act of 1933, 15 U.S.C. 77e (a) and (c), and revised Rule 18 of the Rules of the Court of Appeals for the Fifth Circuit are set forth in the appendix, *infra*, pp. 13–14.

STATEMENT

Petitioners seek review of the court of appeals' affirmance of the district court's order enjoining them from selling securities without registration under the Securities Act of 1933. The district court found that the defendants in each of two offerings had sold "investment contracts" involving claims to oil, gas or other mineral rights in submerged lands off the coast of Santa Barbara, California.

The defendants, doing business as Deep Rock Drilling Company, commenced offering quitclaim deeds to offshore oil lands in March 1968 (JA 22a; R. 61).[1] The deeds were to fractional interests in a 500,000 acre tract to which the defendants and six others had staked some 4,000 mining "claims" with the Santa Barbara County Recorder during the preceding month. A few days after the defendants filed their claims, the Department of the Interior leased the land involved to several oil companies.

As the court of appeals noted (Pet. App. 28–30), in their first offering the defendants said that the money they raised from the sale of these interests would be used for an "expensive court fight" to validate their claim to the land and the indigeneous oil underneath the land (JA 49a; R. 101). They represented that the contemplated "court fight" would inure to the benefit of each purchaser of a 1/16th interest in the defendants' claims. They promised that if they were successful, "* * * each 1/16th interest should realize a payout of about 1,000-to-1" (JA 49a; R. 101). With their offering letter the defendants included a "Legal Synopsis," which set forth the basis for their belief that they would prevail in a court contest with the Department of the Interior over the right to the land (J.A. 50a; R. 102), and newspaper articles quoting one of the defendants' references to the necessity of litigating the validity of the claims (JA 53a; R. 105).

[1] References to the joint appendix of the parties, filed by the Commission, are cited as "JA — a." References to the record before the court of appeals are cited as "R. —."

In April 1968, the Commission's Regional Office in Atlanta notified the defendants that their initial offering appeared to be a "security" within the meaning of the Securities Act and informed them of the registration requirements of that Act (JA 18a–20a, 39a; R. 53–54, 91). The defendants, who have conceded that they had been offering unregistered investment contracts (Pet. 4; JA 22a; R. 61–62), agreed in May 1968 that they would not continue further offerings of such mining claims in violation of the federal securities laws (JA 28a, 106a–107a; R. 66, 194–195).

Later in the same month the defendants commenced a second offering of these mining claims (JA 19a, 135a; R. 53, 243). It differed from the first only in that the defendants offered 1/8th undivided interests, rather than 1/16th undivided interests, and the offering letter contained a paragraph disclaiming any "collaterial [sic] offer, promise or assurance of any nature whatsoever" (JA 62a; R. 114). This second letter, however, referred to the contested nature of the title being sold and to the necessity of litigating title. It also included copies of the same "Legal Synopsis" and newspaper clippings that had been included with the first offering.

Upon learning of the second offering, and after the defendants failed to show the Commission that they had offered to rescind the earlier sales (Pet. App. 18, 29), the Commission commenced the present suit for an injuction. On October 31, 1968, the district court granted a preliminary injunction (Pet. App. 15–21) on the basis of affidavits that were essentially uncontested. The court held that both the first and second

offerings violated the registration requirements of Sections 5(a) and 5(c) of the Securities Act.

Thereafter, counsel for the Commission, pursuant to Rule 36 of the Federal Rules of Civil Procedure, requested the defendants to make certain admissions concerning the genuineness and the receipt or mailing of certain documents and the truth of several statements "for the purpose of this action only and subject to all pertinent objections to admissibility which may be interposed at the trial * * *" (JA 32a–33a; R. 85). The defendants objected to the Commission's request for admissions, claiming that since the preliminary injunction already granted and the permanent injunction sought would be enforceable by criminal penalties, the injunction action "partakes of the nature of a criminal proceeding, and the answering of the requests would be requiring the defendants to testify against themselves, in violation of the fifth amendment to the Constitution of the United States" (JA 73a–75a; R. 129–130).[2] The district court overruled these objections and ordered the defendants to "respond to plaintiff's request for admissions as provided by Rule 36, Federal Rules of Civil Procedure" (App. 76a–77a; R. 132). Thereafter the defendants filed their answers to the request for admissions, admitting that each of the documents was genuine and was either

[2] The defendants' contention was not that the admissions might be used in independent criminal proceedings for the same violations, but rather that they might be used in a possible contempt proceeding for violation of the permanent injunction sought or possibly of the preliminary injunction already obtained (JA 74a; R. 129).

mailed or received by them and admitting the truth of the statements propounded.

A hearing on the Commission's motion for a permanent injunction was held on February 19, 1969 (JA 93a; R. 179). The Commission offered the defendants' admissions into evidence (JA 95a; R. 181) and called as its only witness one of the defendants, Ford M. MacElvain. No objection was interposed specifically with respect to the admissibility of the defendants' response to the Commission's request for admissions, but counsel for the defendant renewed his contention that the proceeding was "in the nature of a criminal proceeding" and objected to Ford M. MacElvain's taking the stand (J.A. 94a–95a; R. 180–181). The court directed that he take the stand, but stated that he could raise his Fifth Amendment claims in response to specific questions that might be asked (JA 95a; R. 181). Neither the defendant nor his counsel objected to any of the questions. Thereafter, the defense itself called the defendant Ford M. MacElvain as a witness (R. 190).

The defendants appealed from the order of the district court granting the permanent injunction, and the record and briefs were filed with the court of appeals. The parties thereafter received written notice, pursuant to revised Rule 18 of the Rules of the Court of Appeals for the Fifth Circuit, that the case was "* * * of such character as not to justify oral argument." Counsel for the defendants filed with the court of appeals a motion to have the case transferred from the summary docket to the regular docket with oral argument permitted. The motion was denied.

The court of appeals thereafter affirmed the judgment, holding that defendants' second offering constituted an offering of an investment contract and thus of a security subject to the registration provisions of the Securities Act (Pet. App. 30–31); that the district court had not abused its discretion in granting a permanent injunction (Pet. App. 32–33); and that the defendants' rights had not been violated by the district court's rulings requiring them to answer the Commission's requests for admission and the defendant Ford M. MacElvain to take the stand as a witness for the Commission (Pet. App. 33).

ARGUMENT

The decision of the court below is correct, and the petition presents no question warranting further review.

1. This Court has repeatedly held that the term "security" as used in the federal securities laws is to be broadly construed. *Tcherepnin* v. *Knight*, 389 U.S. 332; *Securities and Exchange Commission* v. *W. J. Howey Co.*, 328 U.S. 293; *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U.S. 344.

These and numerous other decisions recognize that Congress intended to reach any arrangement which in substance involves a security transaction, regardless of form. *Joiner* noted that "* * * the reach of the Act does not stop with the obvious and commonplace" but extends to "[n]ovel, uncommon, or irregular devices" (320 U.S. at 351). *Howey* further explained that the term "investment contract" "embodies a flexible

rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits" (328 U.S. at 299). This Court there concluded that the "test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." 328 U.S. at 301.

In the instant case, the "management services" (*Howey, supra*, 328 U.S. at 299) are in the form of a promise or proposal to litigate. Such an investment scheme is not novel. See, *Securities and Exchange Commission* v. *Latta*, 250 F. Supp. 170 (N.D. Cal.), affirmed, 356 F. 2d 103 (C.A. 9), certiorari denied, 384 U.S. 940. See, also, *Securities and Exchange Commission* v. *McBride*, 143 F. Supp. 562 (M.D. Tenn.). The courts below, therefore, correctly concluded that the "claims" the defendants were offering for sale in both the first and second offerings were "securities" within the meaning of the Securities Act.

In the circumstances of the repeated violation, the injunction was entirely appropriate. See, *e.g., United States* v. *Parke, Davis & Co.*, 362 U.S. 29, 48; *Securities and Exchange Commission* v. *Keller Corp.*, 323 F. 2d 397 (C.A. 7); *Hillsborough Investment Corp.* v. *Securities and Exchange Commission*, 276 F. 2d 665 (C.A. 1); cf. *Wirtz* v. *Atlas Roofing Mfg. Co.*, 377 F. 2d 112 (C.A. 5); *Opelika Royal Crown Bottling Co.* v. *Goldberg*, 299 F. 2d 37 (C.A. 5).

2. The defendants' constitutional rights were not violated by the district court's rulings that they "respond to plaintiff's request for admissions as provided

by Rule 36" (JA 76a–77a; R. 132) and that the defendant Ford M. MacElvain take the stand as an adverse witness (JA 95a; R. 181). The court properly rejected defendants' sweeping contention that requests for admissions are inappropriate in suits for injunctive relief because the resulting injunctions may be enforced by means of criminal contempt proceedings in which the admissions might be used against a defendant. A contempt conviction, obviously, can be based only on acts which occur after the entry of the injunction—which were not the subject of the requests involved here. Of course, a proper claim of privilege, directed to particular requests for admissions, would have been an adequate response under the judge's order, but the defendants made no such claim (see *supra,* p. 5, n. 2).

The defendant Ford M. MacElvain was not compelled to testify against himself at the hearing on the permanent injunction. The judge ordered him to take the witness stand, stating that the action was not in the nature of a criminal proceeding (JA 95a; R. 181). He then specifically stated to counsel:

> If he wants to raise at the time specific questions are propounded his Fifth Amendment rights regarding self-incrimination, he may do so (JA 95a; R. 181).

The defendant never did so.

3. We adhere to the view, previously urged by the government in this Court,[3] that revised Rule 18 of the

[3] See the Briefs in Opposition in *Ambers* v. *United States*, No. 799, this Term, certiorari denied, January 19, 1970; and *Grayson* v. *United States*, No. 834, this Term, certiorari denied, February 2, 1970. A copy of each of these Briefs in Opposition has been furnished to counsel in the present case.

Rules of the Court of Appeals for the Fifth Circuit, permitting disposition of an appeal on the basis of briefs without oral argument, is valid. In any event, petitioners were not prejudiced by the application of that rule here.

Their appeal to the court below was patently without merit. They concede that their first offering "* * * was an improper offer of an investment security without registration" (Pet. 4) and, as held by both courts below, the changes between that and the second offering were legally inconsequential. Accordingly, the grant of the injunction was proper. And, as previously noted, there is no substance to defendants' argument that a suit for an injunction is not subject to the rules of civil procedure dealing with admissions and testimony of adverse parties because the answers could be used against the defendant in a subsequent contempt proceeding.

Petitioners have not suggested what, if any, additional arguments they would have made had there been oral argument. Nor did they file a reply brief in the court below responding to the cases and arguments in the answering brief of the Commission.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted.

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FEBRUARY 1970.

APPENDIX

SECURITIES ACT OF 1933, AS AMENDED

Section 5(a), 15 U.S.C. 77e(a) provides:

> Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
>
> (1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or
>
> (2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

Section 5(c), 15 U.S.C. 77e(c) provides:

> It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8.

Rule 18 (revised) of the Rules of the Court of Appeals for the Fifth Circuit provides:

SUMMARY CALENDAR

(a) Whenever the court, sua sponte or on suggestion of a party, concludes that a case is of such character as not to justify oral argument, the case may be placed on the summary calendar.

(b) A separate summary calendar will be maintained for those cases to be considered without oral argument. Cases will be placed on the summary calendar by the clerk, pursuant to directions from the court.

(c) Notice in writing shall be given to the parties or their counsel of the transfer of the case to the summary calendar.

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